

STRICTLY CONFIDENTIAL (FR) CLASS I-FOMC

*Material for*  
*Staff Presentation to the*  
*Federal Open Market Committee*

*February 5, 1991*

## **OUTLINE OF THE PRESENTATION**

1. What are the FOMC projections?
2. What has been assumed about the war and its budgetary consequences?
3. What about the credit crunch and other financial stresses?
4. Where is the dollar headed?
5. What might the oil market look like?
6. What if foreign growth were disappointing?
7. What will bring about an economic upturn?
8. Have we turned the corner toward lower core inflation?
9. How fast can the economy grow?
10. What if the Fed were to ease substantially in the near term?

## ECONOMIC PROJECTIONS FOR 1991

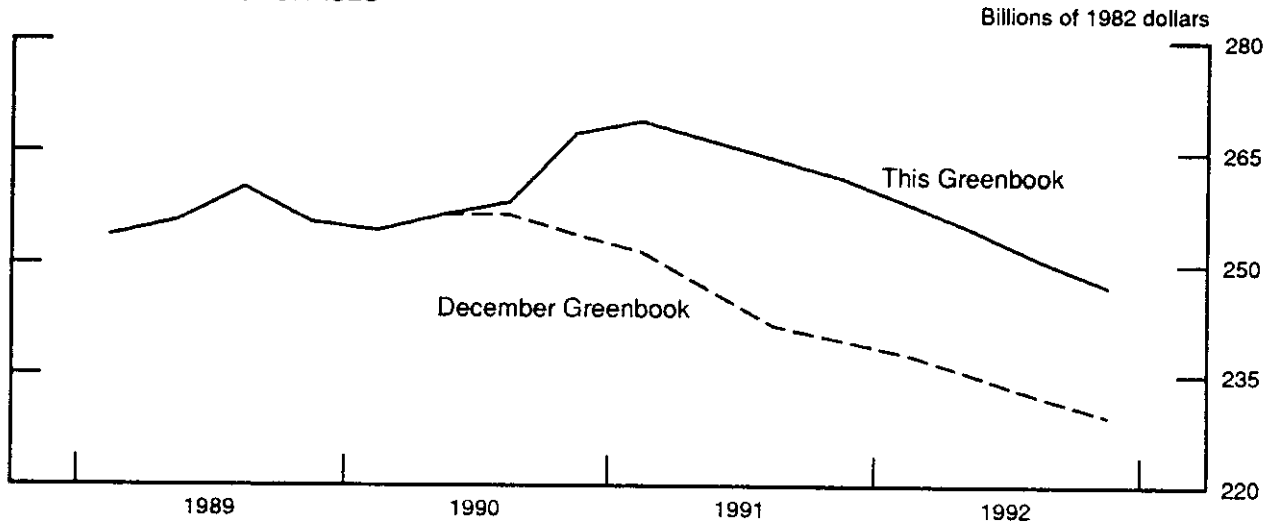
	FOMC			
	Range	Central Tendency	Administration	Staff
----- Percent change, Q4 to Q4 -----				
Nominal GNP	3 <sup>1</sup> / <sub>2</sub> to 6 <sup>1</sup> / <sub>4</sub>	3 <sup>3</sup> / <sub>4</sub> to 5 <sup>1</sup> / <sub>4</sub>	5.3	5.9
<i>previous estimate</i>	3 <sup>1</sup> / <sub>2</sub> to 7	5 <sup>1</sup> / <sub>4</sub> to 6 <sup>1</sup> / <sub>2</sub>	7.2	6.4
Real GNP	- <sup>1</sup> / <sub>2</sub> to 2	<sup>1</sup> / <sub>2</sub> to 1 <sup>1</sup> / <sub>2</sub>	0.9	1.9
<i>previous estimate</i>	0 to 3	1 <sup>3</sup> / <sub>4</sub> to 2 <sup>1</sup> / <sub>2</sub>	2.9	2.2
CPI	3 to 5	3 to 4 <sup>1</sup> / <sub>4</sub>	4.3	3.9
<i>previous estimate</i>	3 <sup>1</sup> / <sub>2</sub> to 5	3 <sup>3</sup> / <sub>4</sub> to 4 <sup>1</sup> / <sub>4</sub>	4.2	4.5
----- Average level, Q4, percent -----				
Unemployment rate	6 <sup>1</sup> / <sub>4</sub> to 7 <sup>1</sup> / <sub>2</sub>	6 <sup>1</sup> / <sub>2</sub> to 7	6.7	6.1
<i>previous estimate</i>	5 <sup>1</sup> / <sub>4</sub> to 7	5 <sup>1</sup> / <sub>2</sub> to 6	5.6	6.1

**THE STAFF PROJECTION**  
(Percent change, annual rate)

	1991				1992			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Nominal GNP	3.3	6.7	6.8	6.7	6.8	6.0	6.0	5.9
Real GNP	-1.5	2.8	3.1	3.1	2.8	2.6	2.5	2.4
CPI	3.4	3.8	4.3	4.1	4.1	4.0	3.8	3.7
CPI excluding food and energy	5.2	4.5	4.7	4.6	4.3	4.1	3.9	3.8
Unemployment rate <sup>1</sup>	6.4	6.4	6.2	6.1	6.1	6.1	6.0	6.0

1. Percent.

# REAL DEFENSE PURCHASES

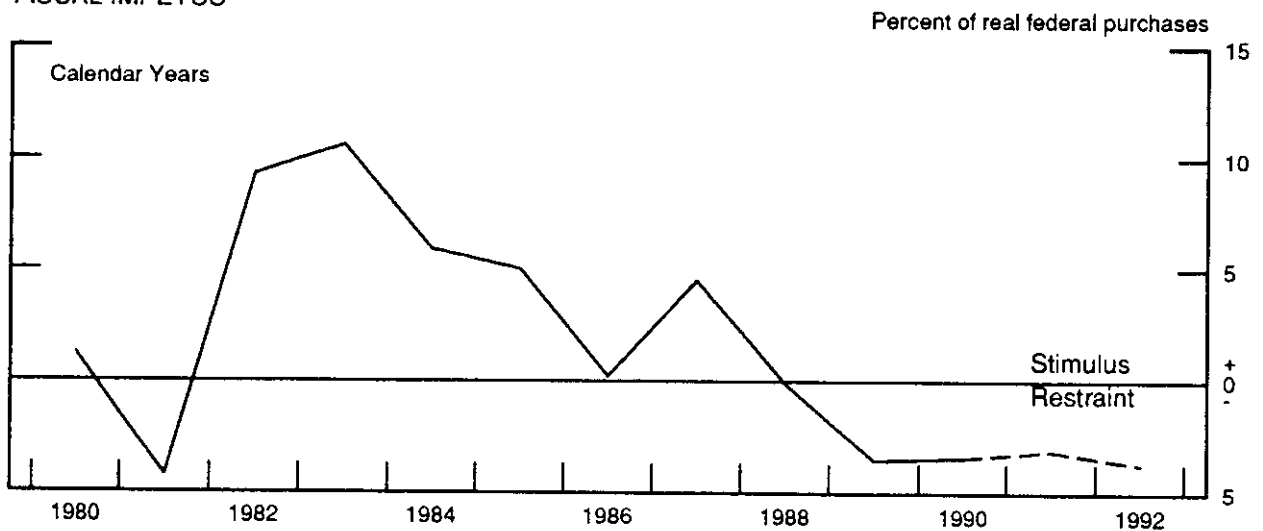


## FEDERAL BUDGET OUTLOOK

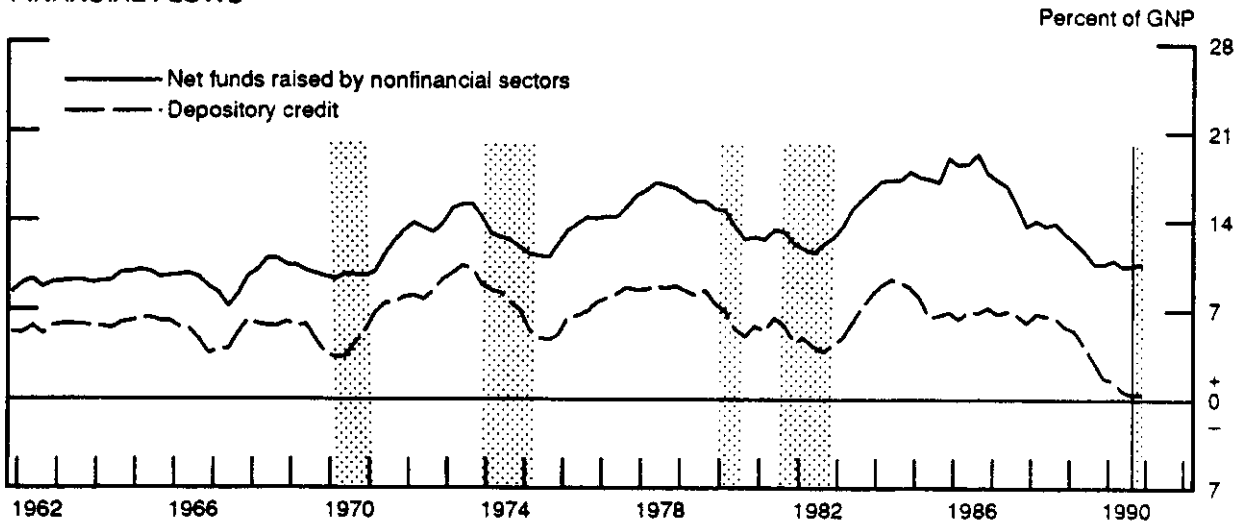
Billions of dollars

	FY1990	FY1991	FY1992
Total deficit	220	283	266
Ex deposit insurance	162	192	172
NIPA deficit	158	165	136

## FISCAL IMPETUS

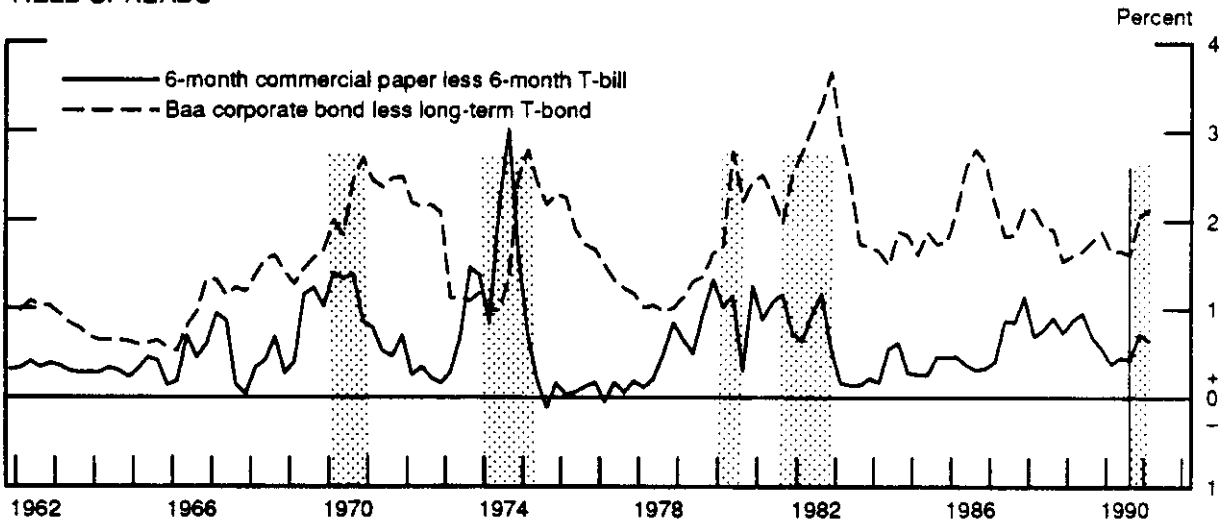


# FINANCIAL FLOWS\*

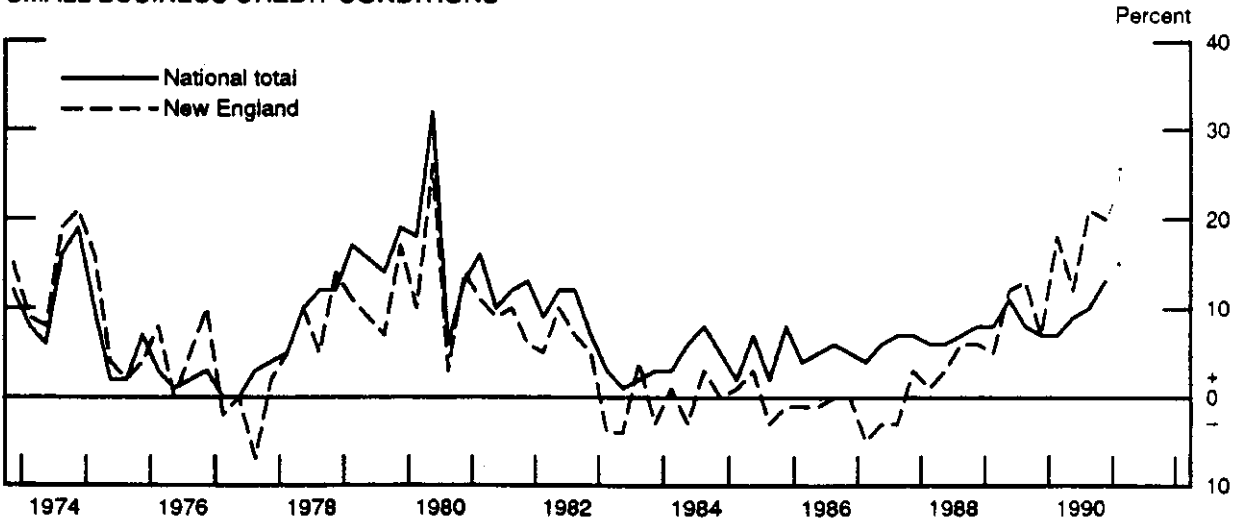


\* Four-quarter moving average, adjusted for RTC.

## YIELD SPREADS



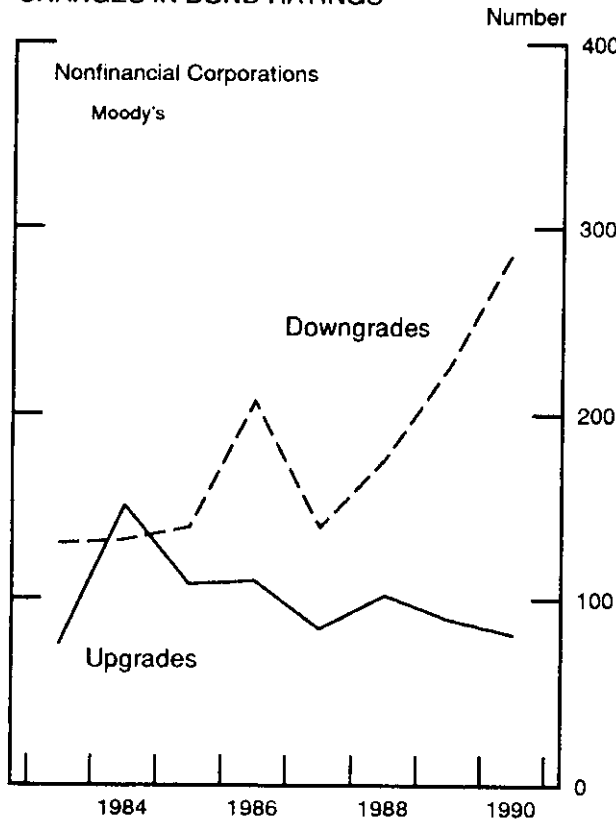
## SMALL BUSINESS CREDIT CONDITIONS \*



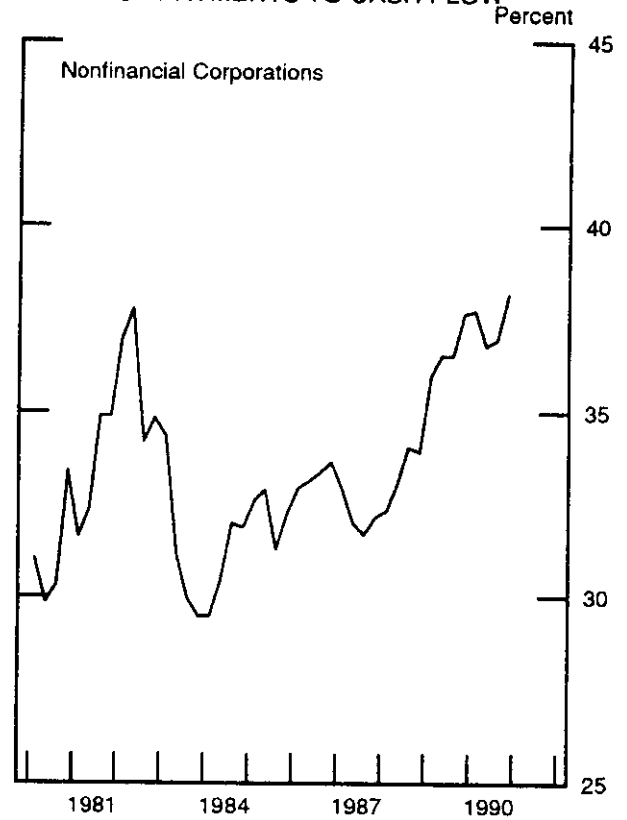
\* Index from the NFIB survey. Credit harder to get minus easier to get.

Chart 5

### CHANGES IN BOND RATINGS

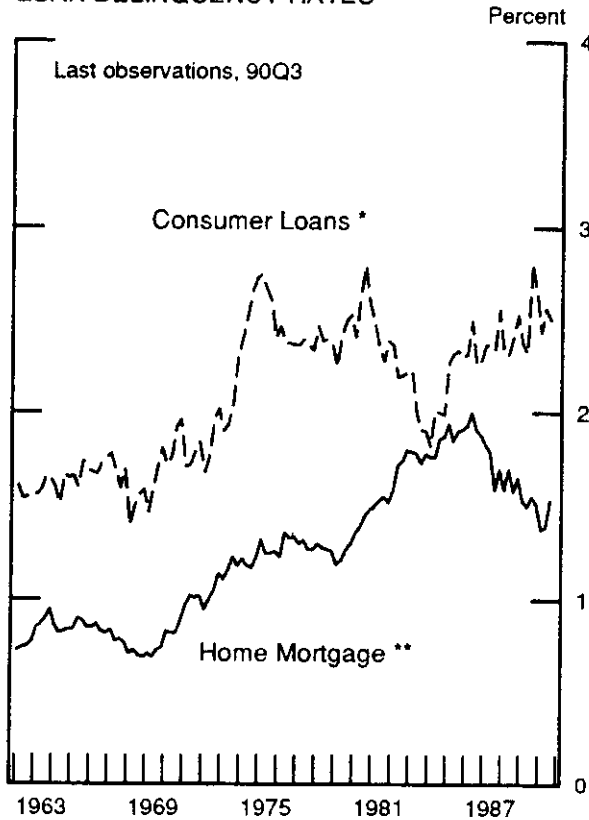


### INTEREST PAYMENTS TO CASH FLOW\*



\* Gross interest to cash flow including interest payments

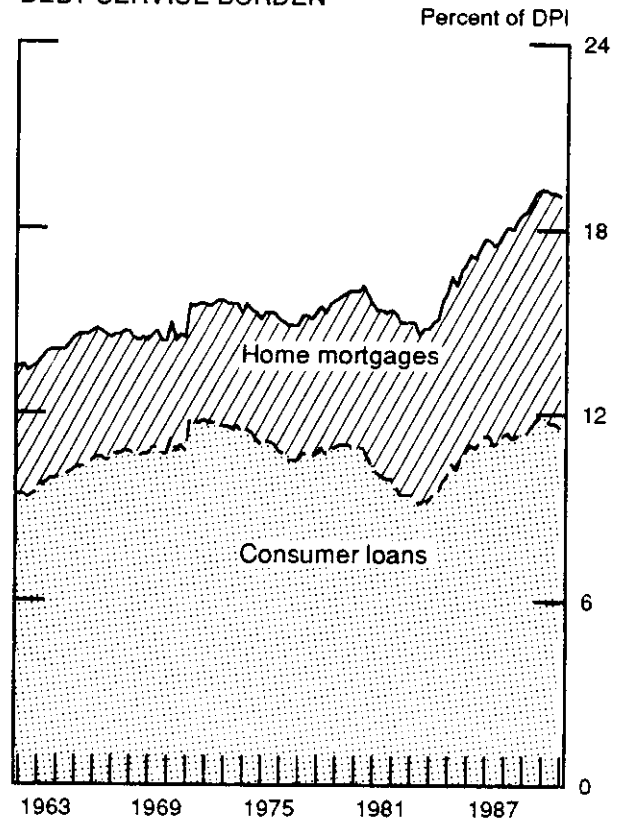
### LOAN DELINQUENCY RATES



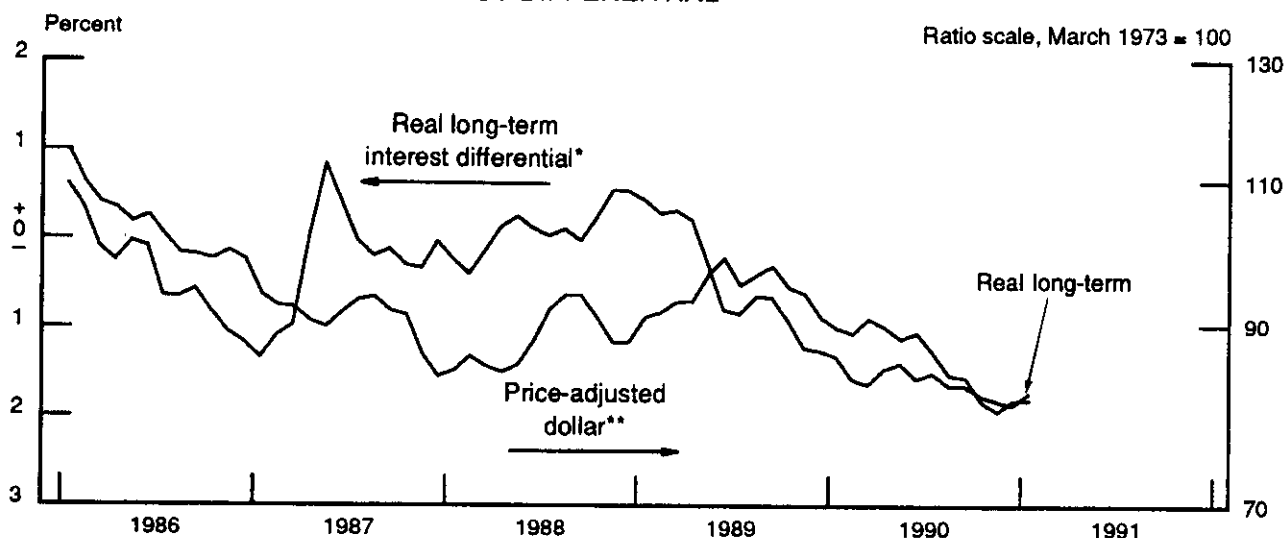
\* Consumer loans overdue 30 days +. ABA series.

\*\* Mortgages overdue 60 days +. MBA series.

### DEBT-SERVICE BURDEN



## THE DOLLAR AND THE INTEREST DIFFERENTIAL



\* Difference between rates on long-term U.S. government bonds and a weighted average of foreign G-10 long term government or public authority bond rates, adjusted for expected inflation.

\*\* Weighted average against foreign G-10 countries, adjusted by relative consumer prices.

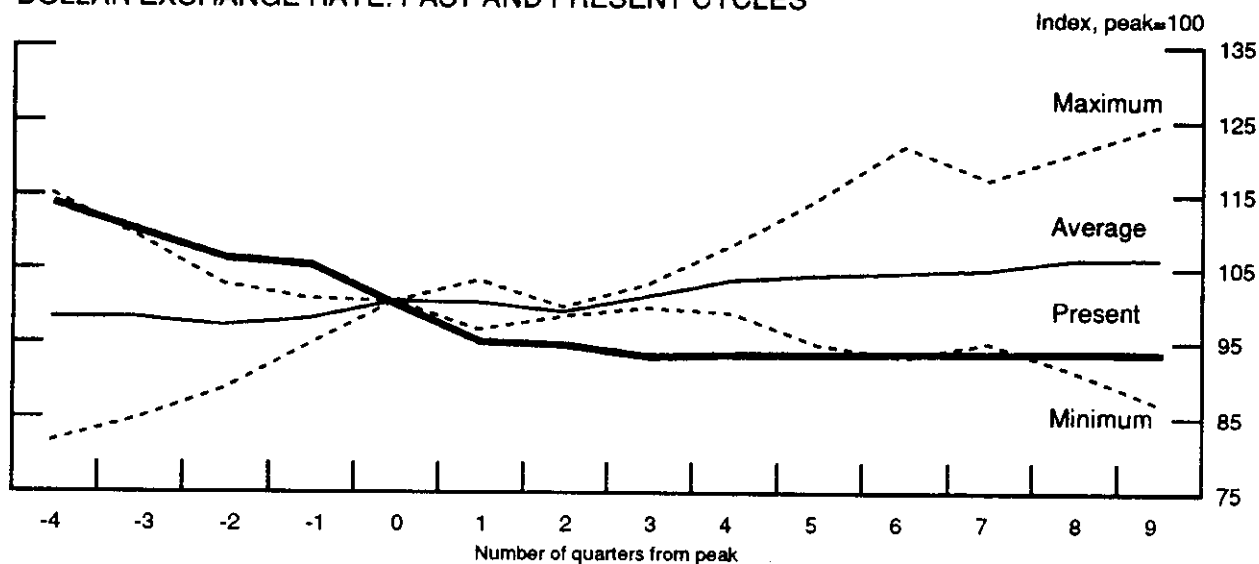
## Nominal Dollar Exchange Rates

	Percent change 6/90 to 2/1/91
Pound Sterling	-13
Deutschmark	-13
Canadian Dollar	-1
Yen	-14
S. Korea	1
Taiwan Dollar	-1

Nominal Interest Rates  
Percent

	Change 6/90 to 2/1/91	Level 2/1/91
Three-month		
Germany	0.9	9.10
Japan	0.8	8.19
U.S.	-1.5	6.75
Long-term		
Germany	-0.2	8.62
Japan	-0.3	6.78
U.S.	-0.6	7.92

## DOLLAR EXCHANGE RATE: PAST AND PRESENT CYCLES\*

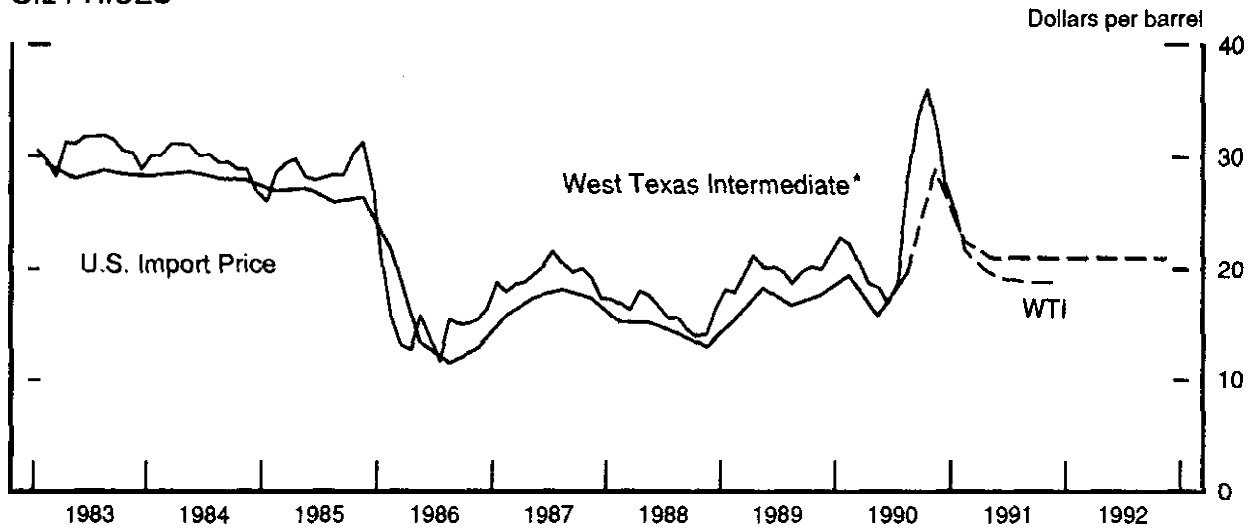


\* Weighted average against foreign G-10 countries. Present and four previous cycles since 1969 are depicted. Peak of present cycle is third quarter of 1990.

Chart 7

## Petroleum and Products

## OIL PRICES



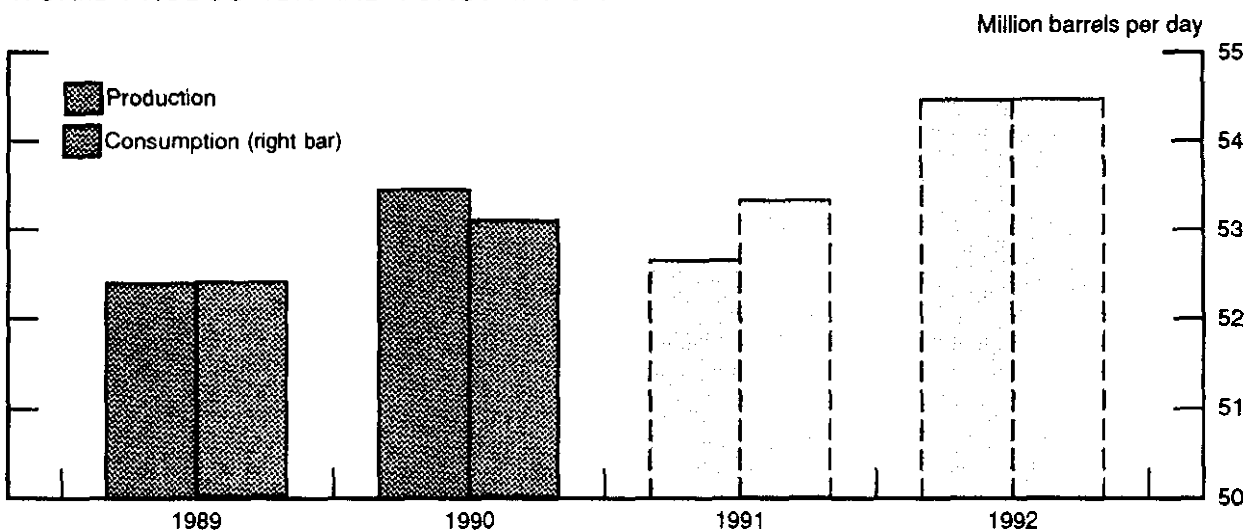
\* Spot prices through January 1991. Future prices February through December 1991

OPEC CRUDE PRODUCTION<sup>\*</sup>  
(Million barrels per day)

	1990-H1	1990-Q3	1990-Q4	1991	1992	OPEC Accord (July)
Total	23.5	21.7	23.1	22.3	24.1	22.5
Saudi Arabia**	5.7	6.5	8.3	8.5	6.9	5.4
Kuwait**	2.0	0.7	0.1	0.0	1.0	1.5
Iraq	3.0	1.4	0.4	0.6	3.0	3.1
Other OPEC	12.8	13.2	14.3	13.3	13.3	12.5

\* Does not include natural gas liquids or lease condensates.

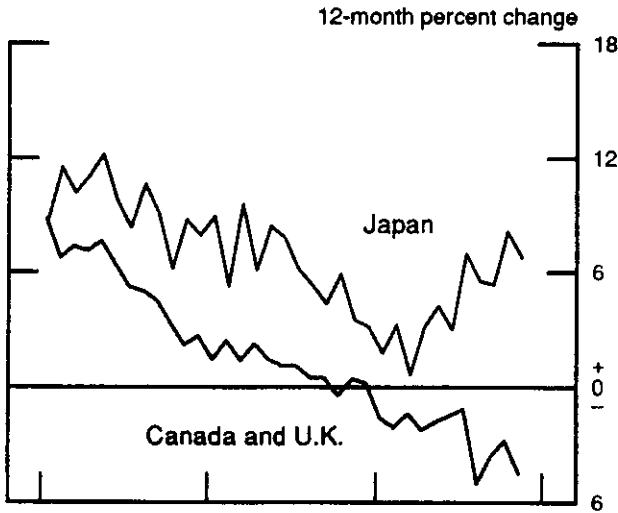
\*\* Includes half of Neutral Zone production through July 1990. Beginning in August, all Neutral Zone production is attributed to Saudi Arabia

WORLD PRODUCTION AND CONSUMPTION<sup>\*</sup>

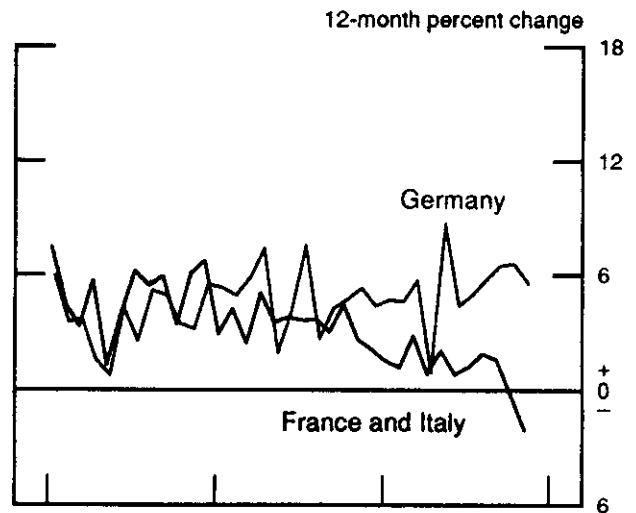
\* Excludes consumption and production consumed in current and former centrally-planned economies.



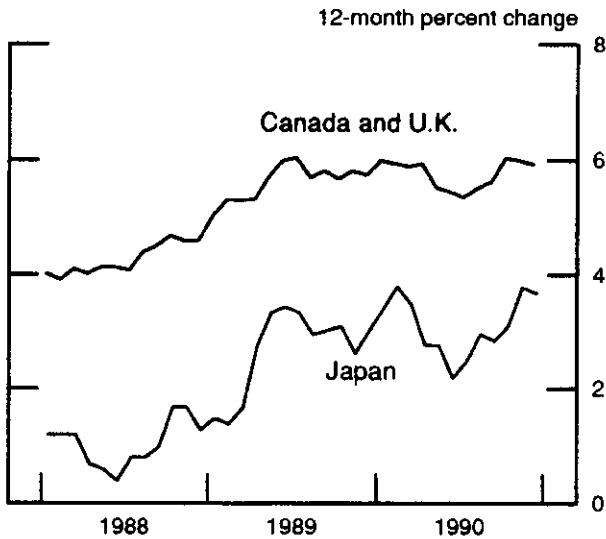
## INDUSTRIAL PRODUCTION \*



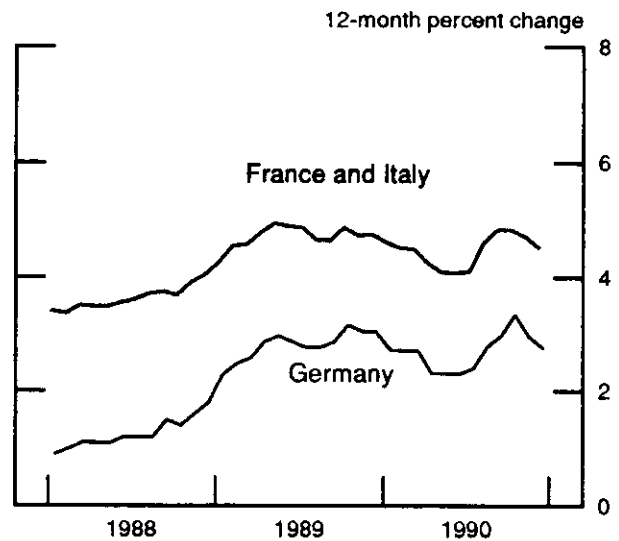
## INDUSTRIAL PRODUCTION \*



## CONSUMER PRICES \*



## CONSUMER PRICES \*

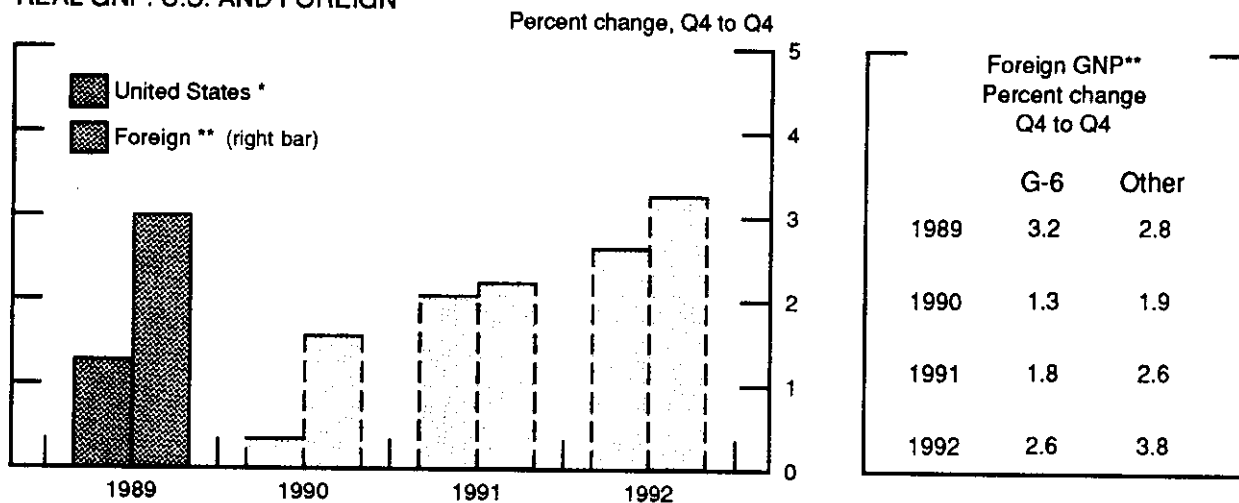


## ECONOMIC POLICY ABROAD

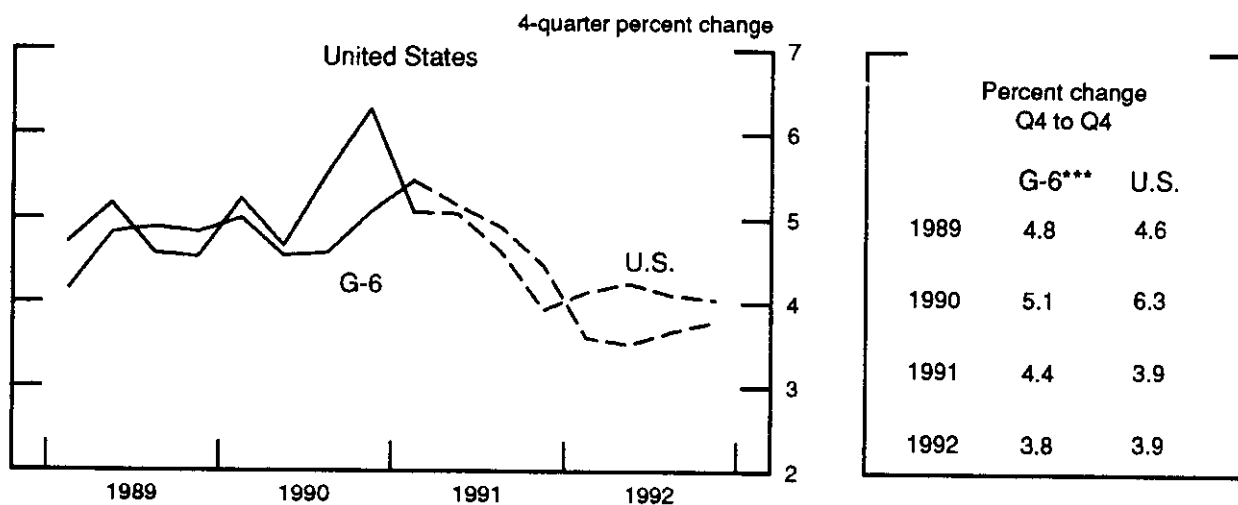
- Inflation has slowed in recent months, but concerns remain; dispersion of growth has widened.
- Monetary policies will be cautious, but interest rates may decline as inflation eases.
- Fiscal policy will be essentially neutral on average, with Germany an important exception.

\* Average using U.S. non-agricultural export weights, 1978-83.

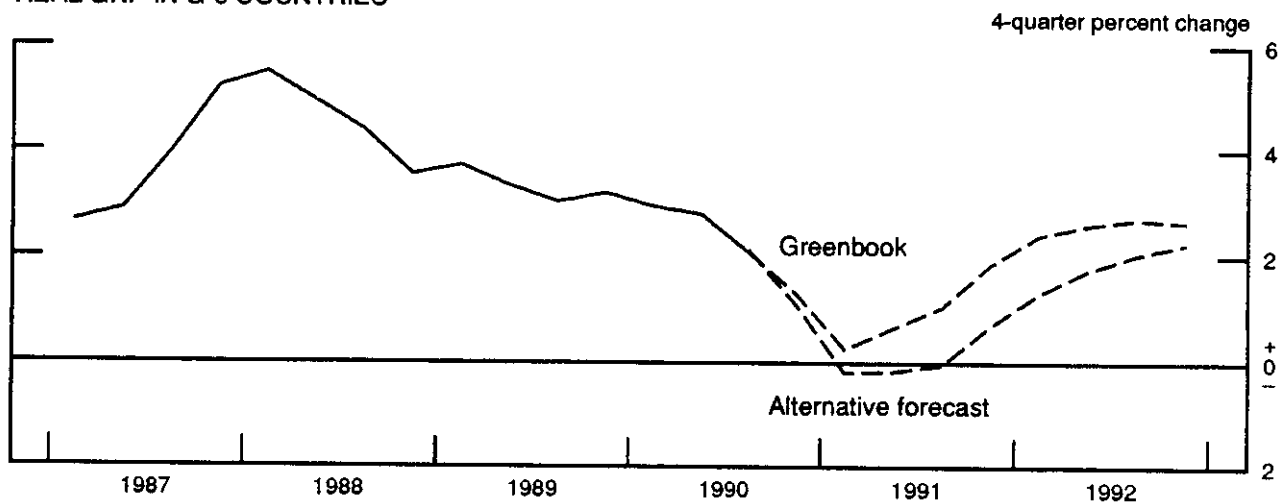
## REAL GNP: U.S. AND FOREIGN



## CONSUMER PRICES: U.S. AND G-6 COUNTRIES \*\*\*



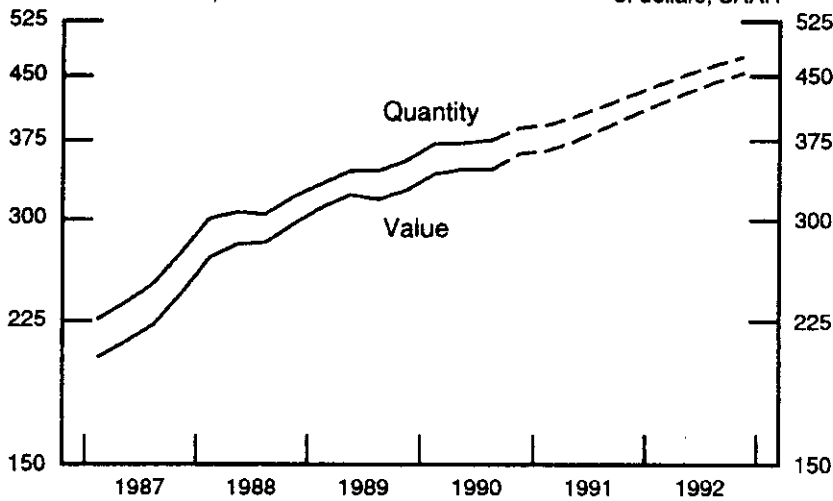
## REAL GNP IN G-6 COUNTRIES \*\*\*



\* Excludes drought effects.

\*\* Average of industrial and developing countries using U.S. non-agricultural export weights, 1978-83.

\*\*\* G-6 average using U.S. non-agricultural export weights, 1978-83.

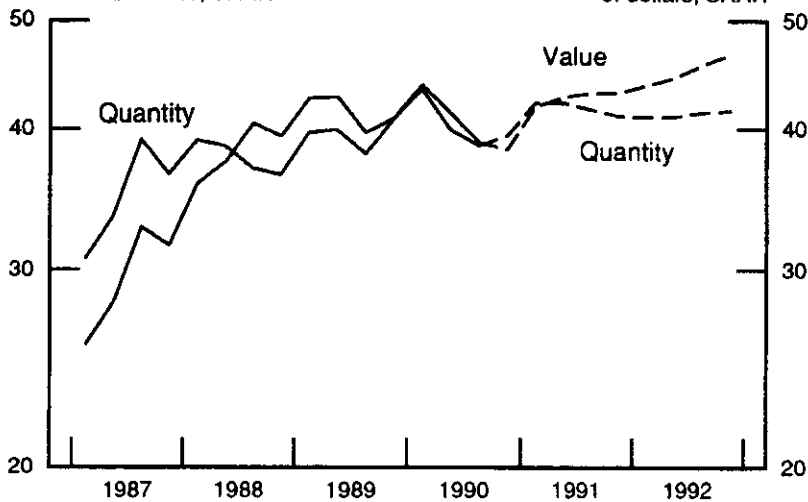
**NON-AGRICULTURAL EXPORTS**Ratio scale, billions  
of 1982 dollars, SAARRatio scale, billions  
of dollars, SAARPercent change  
Q4 to Q4

1990 1991 1992

Value 11 11 13

Price 1 2 1

1982\$ 10 10 11

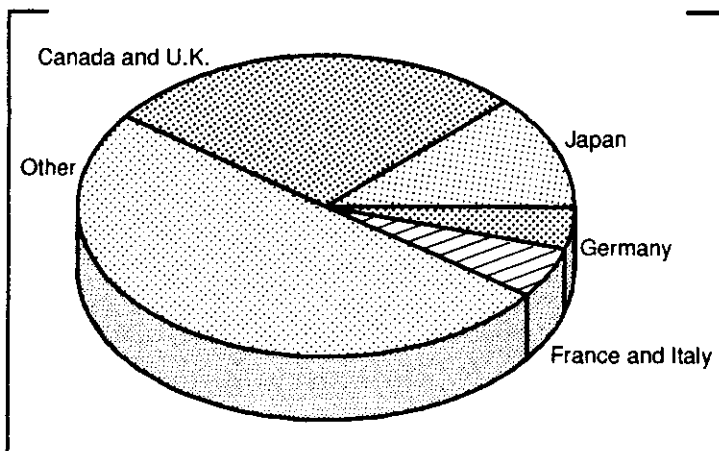
**AGRICULTURAL EXPORTS**Ratio scale, billions  
of 1982 dollars, SAARRatio scale, billions  
of dollars, SAARPercent change  
Q4 to Q4

1990 1991 1992

Value -6 12 8

Price -3 8 7

1982\$ -3 4 1

**SHARE OF U.S. EXPORTS, 1990\***

\* Estimated shares for 1990.

**ALTERNATIVE SCENARIO**Deviation from Greenbook,  
1992-Q4

Billions of 1982\$, SAAR

Exports of goods -10

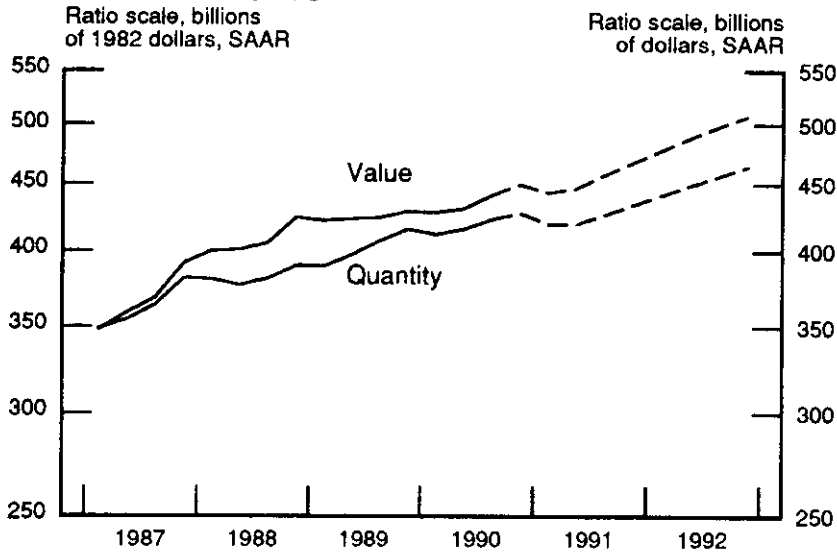
Exports of services -5

Net exports  
(goods and services) -9

Chart 11

**NON-OIL IMPORTS**

Ratio scale, billions of 1982 dollars, SAAR

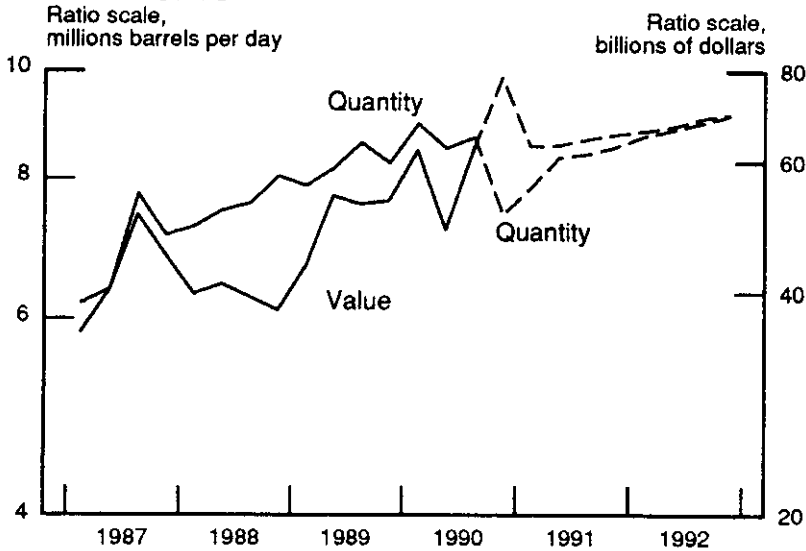
Percent change  
Q4 to Q4

1990 1991 1992

Value	5	4	8
Price	2	2	1
1982\$	3	2	7

**OIL IMPORTS**

Ratio scale, millions barrels per day



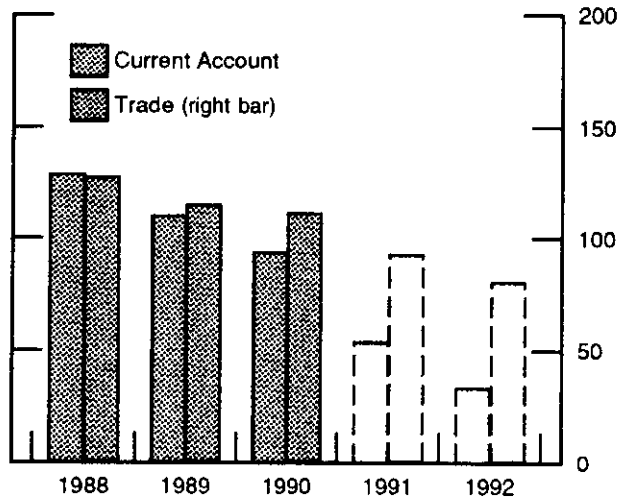
Q4 Level

Price MBD  
(\$/barrel)

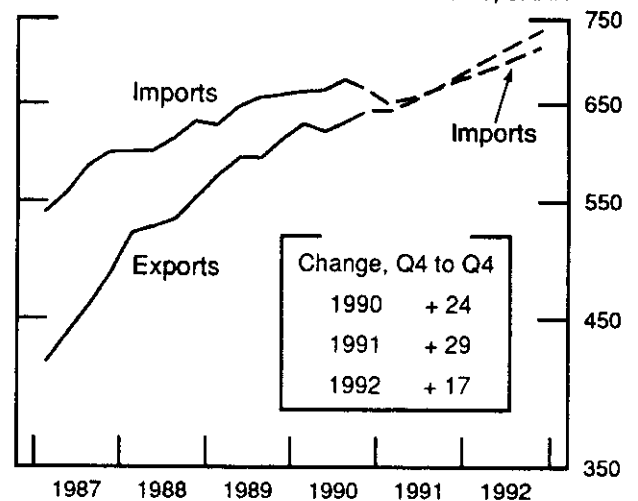
1989	17.67	8.2
1990	28.85	7.4
1991	21.00	8.5
1992	21.00	9.1

**EXTERNAL DEFICITS**

Billions of dollars, SAAR

**REAL NET EXPORTS\***

Ratio scale, billions of 1982 dollars, SAAR

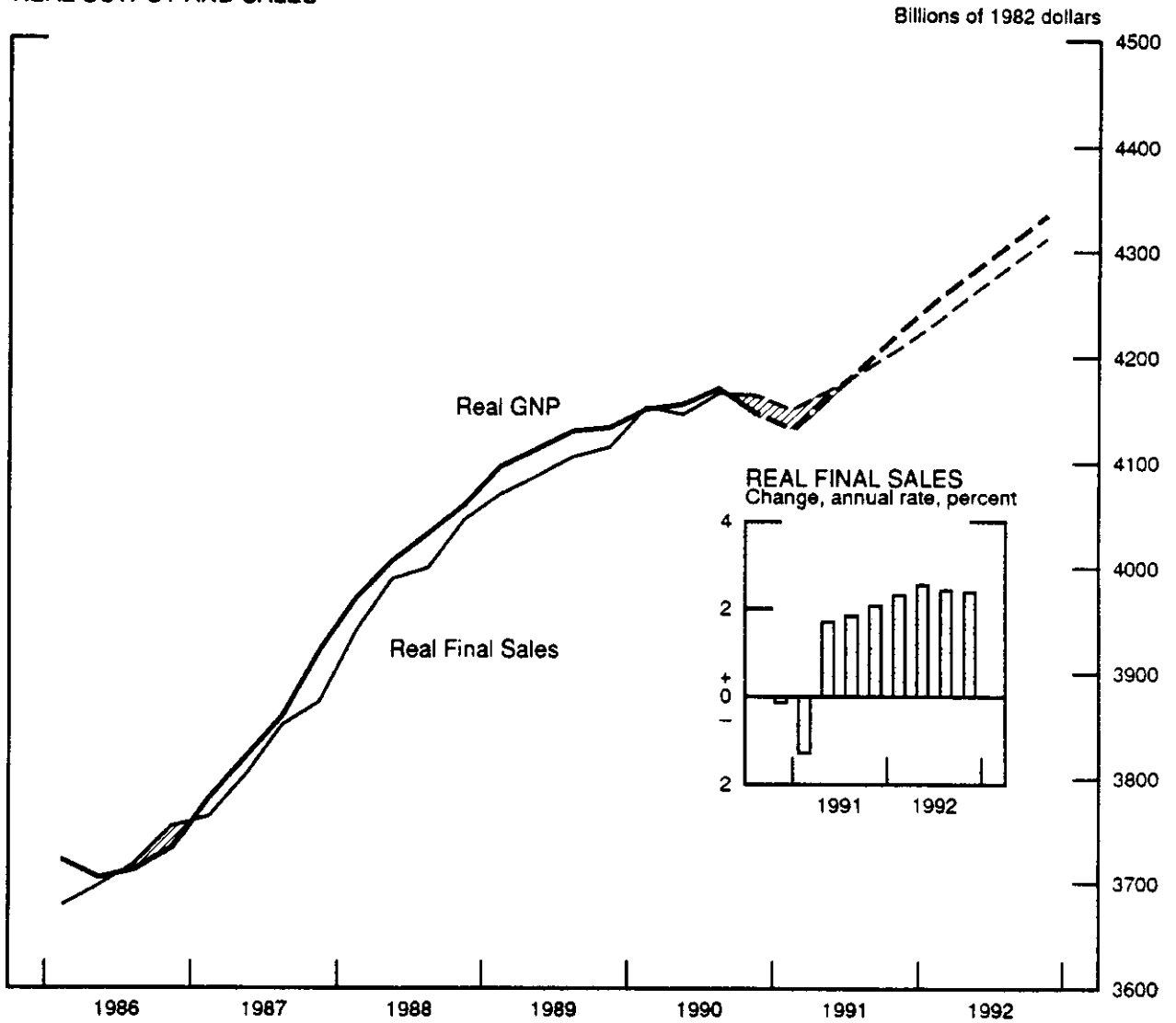


Change, Q4 to Q4

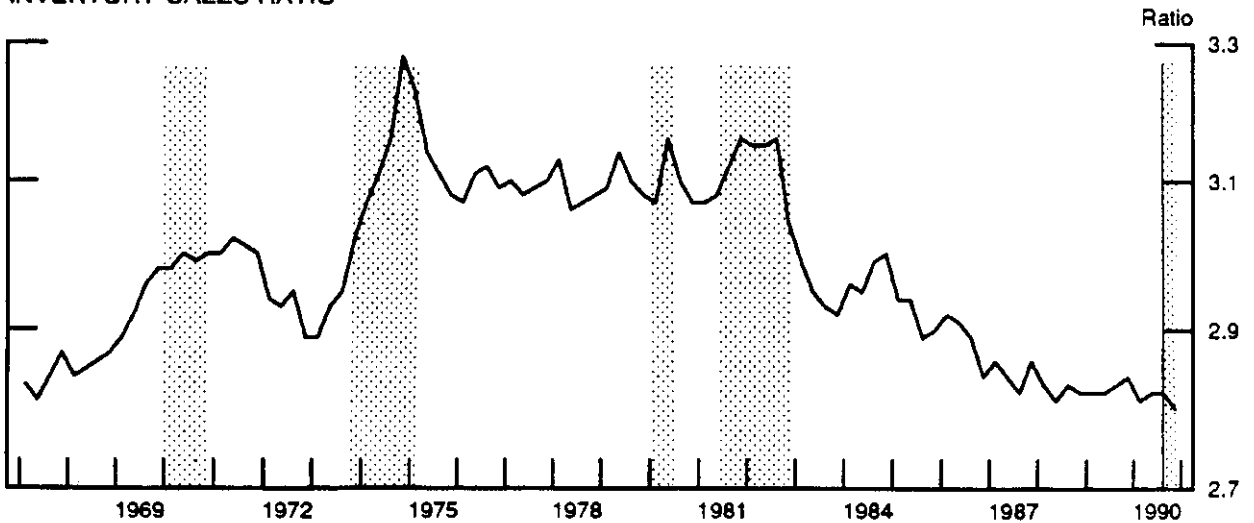
1990	+ 24
1991	+ 29
1992	+ 17

\* Goods and services.

# REAL OUTPUT AND SALES



## INVENTORY-SALES RATIO\*



\* Nonfarm, 1982 dollars.

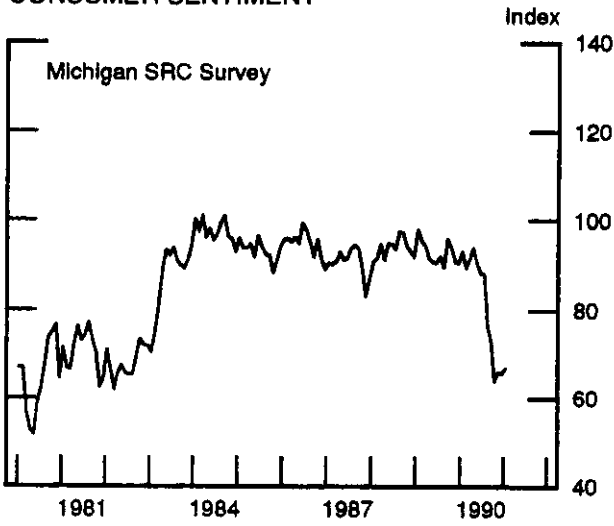
## CONTRIBUTIONS TO REAL GNP GROWTH

	1990	1991			1992
	Q4	Q1	Q2	H2	
	<i>Percent change, annual rate</i>				
1. Real GNP	-2.1	-1.5	2.8	3.1	2.6
	<i>Contribution, percentage points</i>				
2. REAL FINAL SALES	-.1	-1.3	1.7	2.0	2.5
3. Net exports	2.2	1.5	.5	.4	.4
4. Exports	1.1	.0	1.0	1.3	1.4
5. Imports	-1.1	-1.5	.5	.9	1.0
6. Private domestic final purchases	-3.3	-2.9	.9	1.6	2.1
7. Consumption	-2.1	-1.0	1.6	1.2	1.4
8. Residential structures	-.7	-.7	-.1	.3	.3
9. Business fixed investment	-.6	-1.2	-.6	.1	.4
10. Government	1.0	.1	.3	-.1	-.1
11. Defense	.9	.2	-.3	-.3	-.3
12. INVENTORY INVESTMENT	-2.0	-.2	1.1	1.1	.1

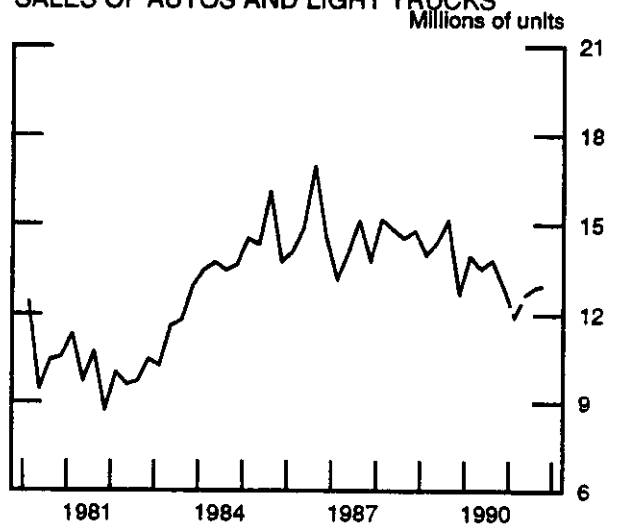
Note: Components may not sum to totals because of rounding.

Chart 14

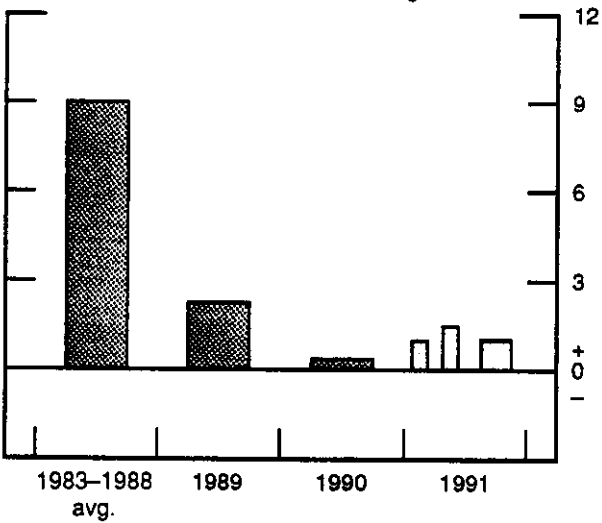
### CONSUMER SENTIMENT



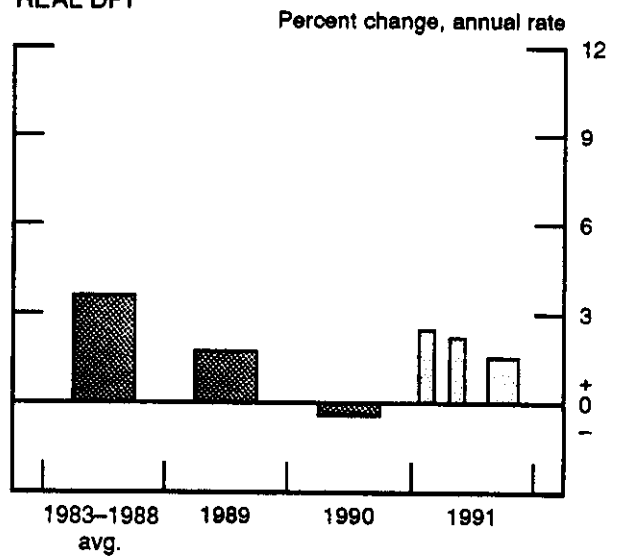
### SALES OF AUTOS AND LIGHT TRUCKS



### PCE DURABLES, EX. MOTOR VEHICLES



### REAL DPI



### AVERAGE MONTHLY MORTGAGE PAYMENT FOR A NEW HOME

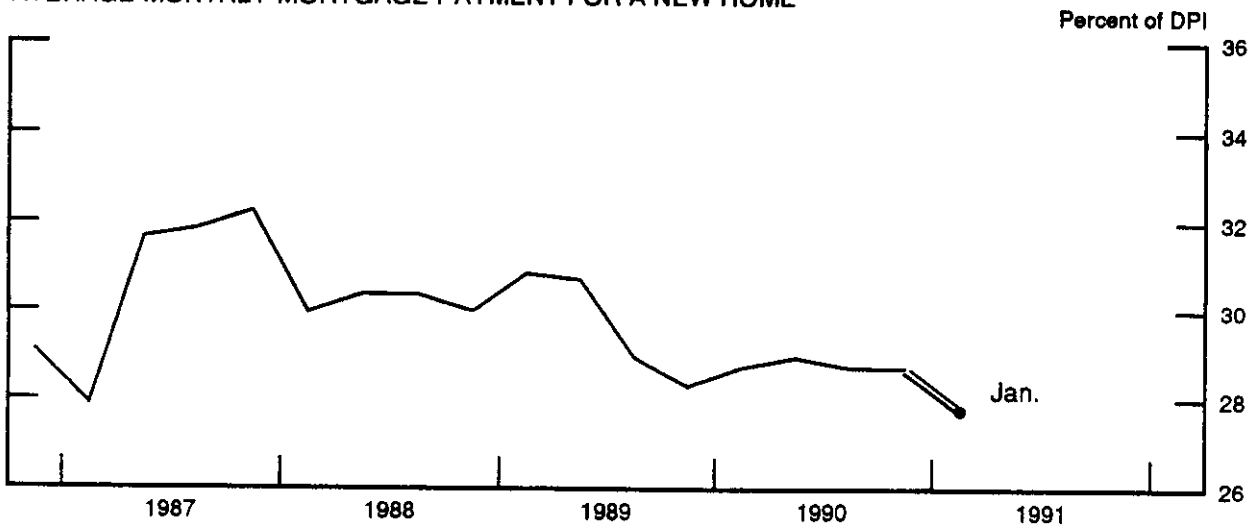
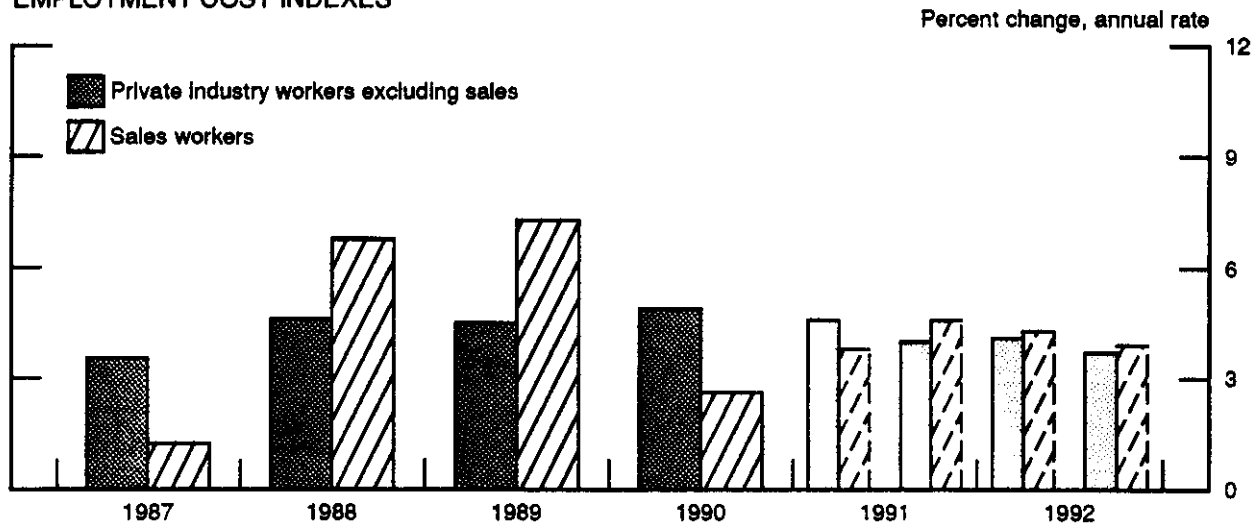


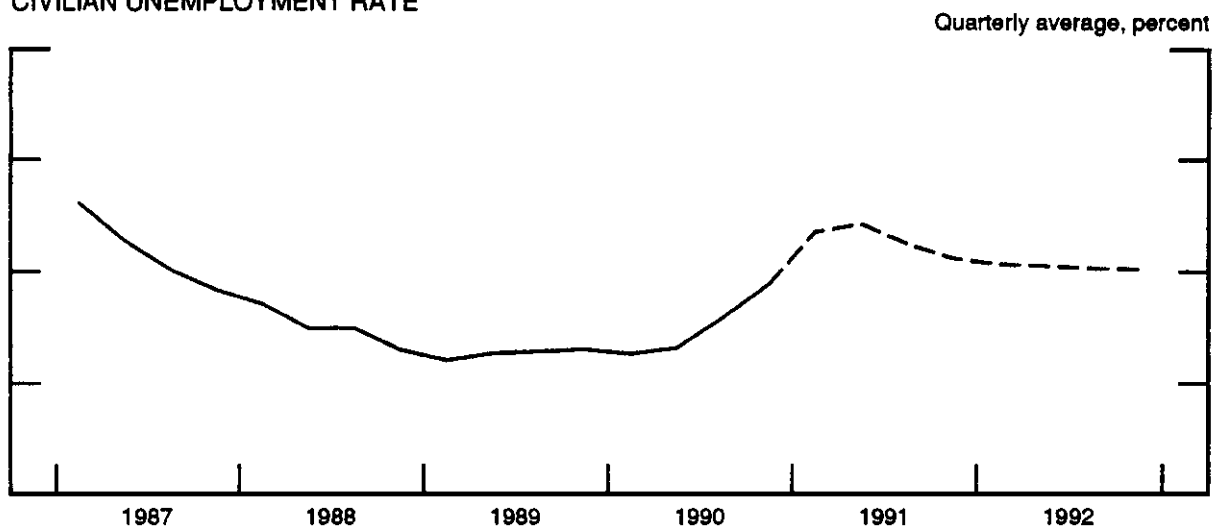
Chart 15

# EMPLOYMENT COST INDEXES\*

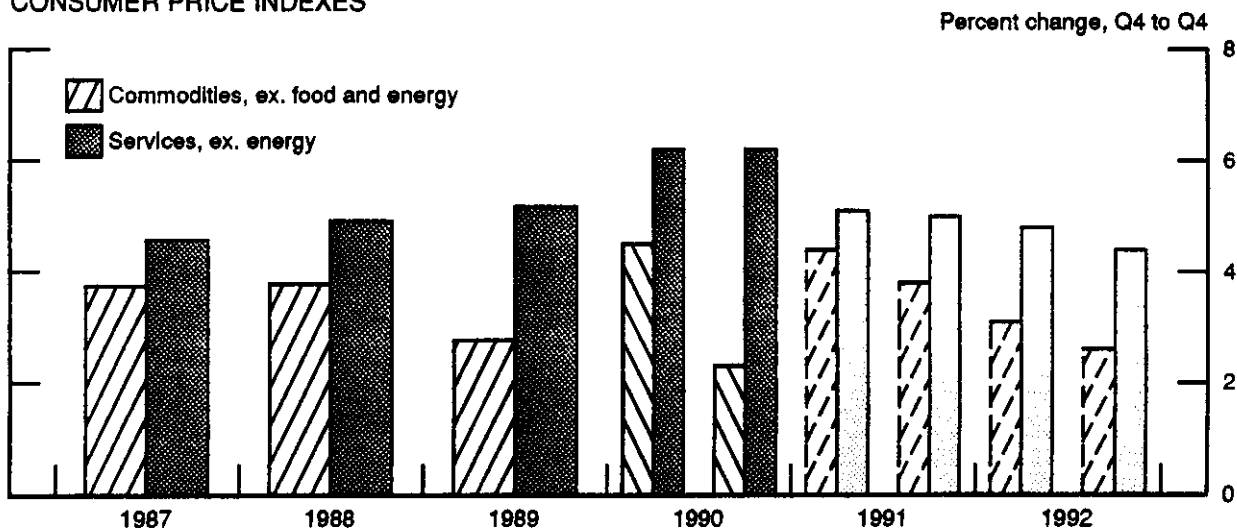


\* Compensation.

## CIVILIAN UNEMPLOYMENT RATE



## CONSUMER PRICE INDEXES





**SUPPLY-SIDE COMPONENTS OF GNP**

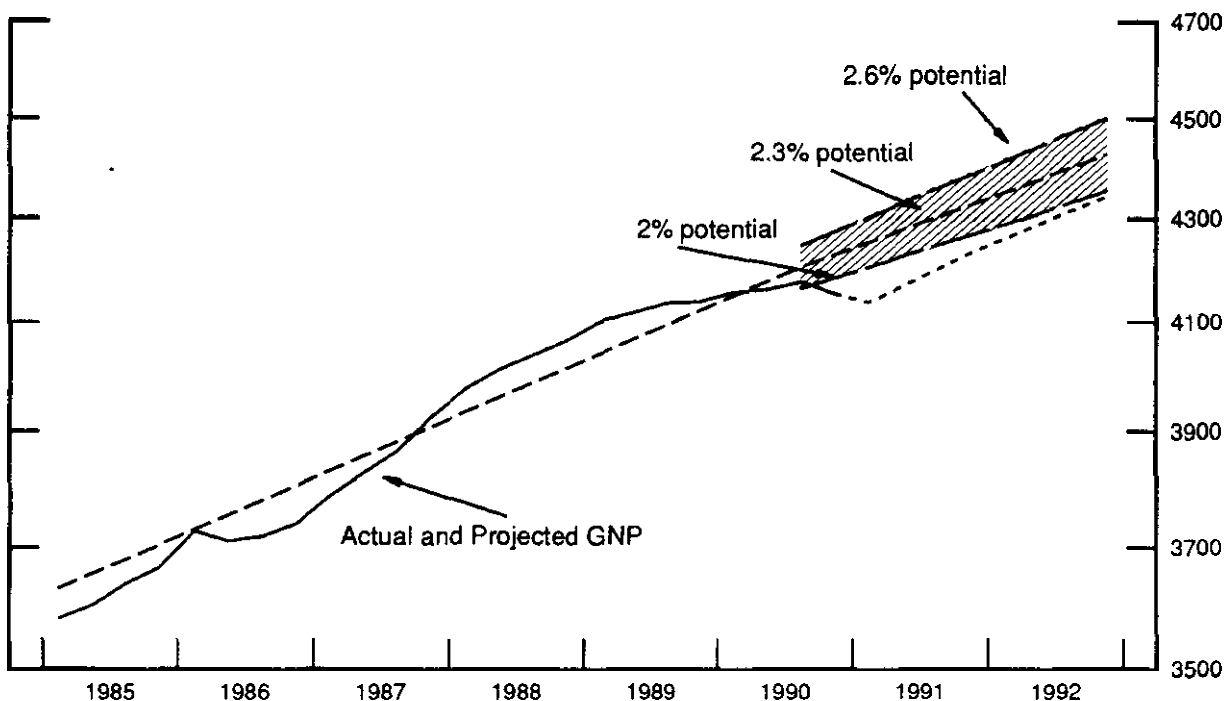
Annual average growth rate

	Long-term trends				Projection
	1948-73	1973-79	1979-89	1989-90	1990-91
1. <b>GNP</b>	<b>3.7</b>	<b>2.6</b>	<b>2.6</b>	<b>1.0</b>	<b>2.3</b>
2. <b>LABOR INPUT</b>	<b>1.2</b>	<b>2.0</b>	<b>1.5</b>	<b>1.9</b>	<b>1.0</b>
3. Working-age population	1.4	1.9	1.2	.9	.9
4. Labor force participation rate	.1	.8	.4	-.1	.3
5. Employment rate	.0	-.2	.1	-.3	.0
6. Average weekly hours	-.4	-.7	-.1	-.3	-.1
7. Technical factors <sup>1</sup>	.1	.1	-.1	1.7	-.1
8. <b>LABOR PRODUCTIVITY<sup>2</sup></b>	<b>2.5</b>	<b>.6</b>	<b>1.1</b>	<b>-.9</b>	<b>1.3</b>
9. Private capital deepening	.8	.7	.7	n.a.	.7
0. Public capital deepening	.2	.0	.0	n.a.	.0
11. <b>TOTAL FACTOR PRODUCTIVITY</b>	<b>1.5</b>	<b>-.1</b>	<b>.4</b>	<b>n.a.</b>	<b>.6</b>
2. Energy	.1	.0	-.1	n.a.	.0
3. Research and development	.4	.2	.2	n.a.	.2
4. Education and experience	.2	.0	.3	n.a.	.4
5. Other	.8	-.3	.0	n.a.	.0

1. Technical factors include; the ratio of GNP to the output of the nonfarm business sector; the ratio of nonfarm business employment to household employment; and rounding error.

2. Nonfarm business sector

n.a. Not applicable



# WHAT IF THE FED WERE TO EASE SUBSTANTIALLY IN THE NEAR TERM?

**SCENARIO 1:** FOMC judges, correctly, that the economy is "one percent weaker" than Greenbook suggests; it lowers fed funds rate to achieve the same output level in late 1992 as in the Greenbook.

**SCENARIO 2:** FOMC judges, incorrectly, that economy is weaker than Greenbook suggests; it eases now, but realizes by midyear that the Greenbook was right and reverses course to avoid seriously overshooting the Greenbook output path in 1992.

	1991	1992
<b>Real GNP, Q4/Q4</b>		
Greenbook	1.9	2.6
Scenario 1	1.6	2.9
Scenario 2	2.3	2.2
<b>Unemployment rate, Q4</b>		
Greenbook	6.1	6.0
Scenario 1	6.2	6.0
Scenario 2	6.0	6.0
<b>CPI, Q4/Q4</b>		
Greenbook	3.9	3.9
Scenario 1	3.9	3.8
Scenario 2	3.9	4.0

	1991				1992			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<b>Federal funds rate</b>								
Greenbook	6.75	6.75	6.75	6.75	6.75	6.75	6.75	6.75
Scenario 1	6.25	5.0	5.0	5.0	5.25	5.5	6.0	6.75
Scenario 2	6.25	5.0	6.25	7.5	8.0	7.75	7.25	6.75